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SUBJECT: JFTC Flexes Its Muscles on Bid-rigging

REF: A) Tokyo 597, B) 05 Tokyo 4642

11. (SBU) Summary: Japan's chief competition regulator, the Japan Fair Trade Commission (JFTC), has made a good start in applying the new powers it gained at the beginning of the year in several bid-rigging cases. Though not a player in what has been arguably the most prominent bid-rigging case in 2006 so far -- one involving a subsidiary of the Japan Defense Agency -- the JFTC has utilized its new leniency program and its enhanced investigatory powers in a number of other high profile cases. The danger now, according to one of Japan's leading competition law experts, is that the JFTC, long considered one of the weaker agencies of the Japanese government, may not have the human resources to meet the challenge of its new authority. This could offer an opportunity to the opponents of a stronger Japanese competition regime to roll back the gains made in 2005 with the amendment of Japan's main antitrust law. End summary.

JFTC Joins the Big League

12. (U) Since the beginning of 2006, Japanese media have revealed several high-profile bid-rigging cases. The most prominent of these has been a series of cases surrounding projects contracted by the Defense Facilities Administration Agency (DFAA), including a number of facilities utilized by U.S. Forces Japan. (Ref A) Although significant in scale -- with a total loss due to collusion estimated at nearly USD 113 million at the current exchange rate -- and in political impact, the DFAA cases, which have fallen under the auspices of the Tokyo District Public Prosecutors' Office have not, to date, involved the

main competition regulator, the Japan Fair Trade Commission. (Note: The lower level of JFTC involvement probably stems from the fact that the charges raised in the DFAA case have centered more on official corruption and less on collusive behavior by private companies. End note.)

13. (U) Of potentially greater significance to long-term progress in the fight against bid-rigging are a separate series of cases where the JFTC has taken a leading role so far this year. These are:

-- Projects for the construction of sewage treatment plants in the Osaka area tendered by municipal governments and valued at over JPY 100 billion.

-- Floodgate projects contracted by both the central and local governments valued at JPY 70 billion

-- Installation of ventilation fans in highway tunnels tendered by the Ministry of Land, Infrastructure, and Transport and the former Metropolitan Expressway Public Corporation (subsequently privatized into the Metropolitan Expressway Co. and the West Nippon Expressway Co.) and valued at JPY 22 billion.

14. (SBU) Each of these three cases represents a new step forward in the JFTC's efforts to prosecute bid-rigging using the new tools at its disposal following the implementation of last year's amendments to the centerpiece of Japan's antitrust legislation, the Antimonopoly Act (AMA). In the floodgate and tunnel ventilation fan cases, for example, some of the

TOKYO 00002905 002 OF 005

companies involved in the bid-rigging scheme reportedly took advantage of the JFTC's new program of leniency under which they could escape some or all surcharges levied by the Commission in exchange for providing evidence against their partners in collusion. (Note: The JFTC does not comment on or confirm reports regarding participation in the leniency program - although presumably the details will emerge when penalties are announced. End note.)

15. (U) In the sewage treatment plant case, the JFTC, in what may be its boldest move, undertook a criminal investigation of the companies concerned, a function that, until the implementation of the 2005 AMA amendments was the sole province of Japan's elite public prosecutors. Japanese media on May 23 revealed that the JFTC had issued formal criminal accusations (kokuhatu) against 11 companies involved in the scheme, effectively turning the case over to the government prosecutors and opening the way for the arrests of the relevant company executives. While JFTC has long had the power to file criminal charges, its new ability to obtain a warrant and collect evidence admissible in court should make it easier for government prosecutors to accept and prosecute AMA violation cases.

Other Agencies Act on Bid-rigging...To a Point

16. (U) The Japanese government will also be considering new contracting guidelines aimed at increasing the application of competitive bidding procedures by all ministries and not just the Ministry of Lands, Infrastructure, and Transport (MLIT), the traditional focus of measures to reduce bid-rigging. On May 11, according to Japanese press reports, the "liaison committee" of Japanese central agencies that issue public works contracts agreed to apply competitive bidding for all contracts except those in

which there is "clearly only a single contractor" and to review all contracts currently being processed in order to issue a plan in June that will identify those contracts that will be converted to competitive bidding. That decision followed a May 10 meeting of the Central Construction Commission, an MLIT advisory body, that recommended revision of the guidelines for bidding and contracting of public works projects in order to expand the scope of competitive bidding at both the central and local levels. According to press reports, this proposed amendment to the MLIT guidelines would be the first in five years.

¶17. (SBU) Despite these measures, however, media reports continue to indicate that bid-rigging tied to the longstanding practice of "descent from Heaven" (amakudari), by which senior bureaucrats assume post-retirement employment at government contractors, persists. Several of the major bid-rigging scandals in 2006 to date -- most notably the DFAA and floodgate incidents -- involved retired government officials, according to media reports. An MLIT official in charge of construction market access confirmed to econoff that, due to the right to choose one's employer enshrined in the Japanese Constitution, MLIT guidelines on reemployment aimed at limiting collusion could only be made voluntary. Retiring officials could ignore the guidelines if they chose to do so. (Note: Japan's National Civil Service Law does stipulate that central

TOKYO 00002905 003 OF 005

government employees are prohibited for two years following retirement from taking jobs at profit-making corporations that have strong relationships with governmental organizations where they worked in the five years before retirement. End note.)

Environment Favors Stronger Competition Regime

¶18. (SBU) Commenting on the JFTC role in these recent cases, Keio University competition law expert Jiro Tamura noted that, unlike the leniency program, which is fundamentally a passive activity for JFTC, actually undertaking a criminal investigation, as in the sewage treatment plant case, "takes guts" because it requires the JFTC to play in the same legal league as Japan's elite prosecutors. In the big cases of 2005, Tamura noted, the JFTC had generally taken action against AMA offenders following moves by the prosecutors. He added that for their part the prosecutors, after years of focusing on political figures, had taken on a new interest in economic crime. He pointed to the arrest and prosecution of the flamboyant Internet entrepreneur and investor Takafumi Horie (Livedoor Co.) as an example of the prosecutors' new interest in the business world.

¶19. (SBU) Tamura credited JFTC Chairman Kazuhiko Takeshima as being very eager to energize the Fair Trade Commission right from the start of his tenure in ¶2002. He indicated that if Takeshima's concrete progress in increasing JFTC enforcement activities had lagged his rhetoric, that was due in large part to the delays and difficulties in achieving passage of the amended AMA, a critical tool if the JFTC were to have "teeth." Now, however, with the amended law in effect and the new contest with the prosecutors in pursuing criminal activity, the JFTC could not return to its previous low-profile status, Tamura noted.

¶10. (SBU) The leniency program of the amended AMA also was forcing changes in the code of conduct for Japan's attorneys, Tamura said. Previously, lawyers for companies accused of bid-rigging would freely share

information among themselves in a common effort to determine what evidence the JFTC might have in a particular case. Now, with the incentive of leniency available, companies were seeking to behave more independently and to force their lawyers to sign binding confidentiality agreements. Bid-rigging cartels, he noted, had been held together as much by threat of retaliation from the other members of the cartel as by common interest, and companies frequently looked for ways to cheat on their ostensible partners. The onset of the leniency program gave those who wanted to escape from an unwelcome decision by their cartel partners a new way to do so.

¶11. (SBU) In addition, Tamura indicated, the application of the law preventing government officials from participating in bid-rigging schemes (Kansei Dango Boshi Ho) and the strict application of suspension from bidding by MLIT on AMA violators -- a reaction in part to the strong public outcry over 2005's headline-generating steel bridge case (ref B) -- have meant that more and more companies were deciding to compete fairly. The bidding suspension, which had previously been negotiable between MLIT and the firms, had inflicted real economic damage on some of the offending

TOKYO 00002905 004 OF 005

firms, Tamura said.

¶12. (SBU) Tamura was skeptical that much would change in the near term with respect to the phenomenon of amakudari. He guessed that the Japanese agencies concerned believed they had taken adequate measures to address the problem. He indicated that more attention might usefully be applied at the other end of the employment process: recruitment. People with little practical experience but who had graduated from elite universities and scored highly on their civil service exam dominate the ranks of the Japanese bureaucracy, Tamura stressed. Mid-level recruitment and mobility to and from the private sector, Tamura said, would greatly benefit the entire government and particularly relatively less prestigious agencies like the JFTC, which had always had to accept the weaker applicants for government service, with the cream of the crop going to more powerful institutions like the Ministries of Finance and Foreign Affairs. Private attorneys on two-year appointments at the JFTC had proven helpful but, because of their short tenure at the agency, had had less of an impact than if they had been able to become career staff.. [As a practical matter, how would JFTC hope to hold on to good lawyers for the long term? New personnel track?]

Higher Expectations: The Danger of Success

¶13. (SBU) Strengthening the human resources of the JFTC, Tamura stressed, was absolutely essential with respect to criminal prosecutions where the JFTC actions would be subject both to comparison with and to scrutiny by the government prosecutors. Right now, the JFTC staff are working seven days a week to process their cases, according to Tamura. One major error in processing a criminal case could, however, derail all of JFTC's other achievements by handing the opponents of the strengthened AMA (e.g., politicians from rural areas, conservative business leaders) evidence to question the agency's fitness to handle its new authority. With a January 2008 review of the 2005 AMA amendments mandated in the revised law itself, these elements have a ready opportunity to take advantage of any egregious error by the JFTC. Tamura noted that a number of companies were already challenging the agency by fighting JFTC's surcharge orders, which the JFTC, in

order to maintain its own authority, had to resist.
(Note: The amended AMA raised the maximum rate of surcharges the JFTC could levy on firms as "compensation" for illegal profits attained through anticompetitive behavior from six percent to 10 percent of a company's income during the period it was engaged in the illegal activity. End note.) The workload and the risk were such at present that many JFTC officials, Tamura said, were scared that a serious mistake in pursuing a case was likely.

Who Will Be JFTC's Champion After Koizumi?

¶14. (SBU) In addition, Tamura was concerned that the JFTC would lose its political support once Prime Minister Koizumi steps down in September. In Tamura's view, Chief Cabinet Secretary Shinzo Abe, if he became Prime Minister, would not pursue reform as aggressively as Koizumi has. Abe, he said, was much more concerned

TOKYO 00002905 005 OF 005

about protecting himself and less likely to take political risks than Koizumi. Former Chief Cabinet Secretary Yasuo Fukuda, he believed, would be more

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likely than Abe to support Japan's competition authorities but would still not equal the strong backing received during Koizumi's tenure. (Note: The five-year term of JFTC Chairman Takeshima will also finish in 2007, thus giving Koizumi's successor an early opportunity to put his own stamp on the agency. End note.)

Comment

¶15. (SBU) Bearing in mind Prof. Tamura's observations regarding the potential dangers of moving too aggressively, the JFTC appears to be off to a good start in applying its new powers. Certainly, based on our reading of the frequent media commentary concerning the unending revelations of bid-rigging and public-private collusion, popular support for JFTC action against bid-rigging remains strong. The primary task for that agency, and for those who want to see it assume a more prominent role in bringing about economic reform in Japan, is to grow into its newly realized authority. JFTC, though, may need to grow up fast as the elements opposed to a stronger competition regime in Japan may be postponing their counterattack until a possibly more auspicious post-Koizumi era.

Schieffer